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SUBJECT: KURDISTAN REGION'S INVESTMENT LAW ATTRACTS LITTLE
FOREIGN DIRECT INVESTMENT TO DOHUK

REF: BAGHDAD 2844

¶1. (U) This is a Kurdistan Regional Reconstruction Team (RRT) cable.

¶2. (SBU) BEGIN SUMMARY: The Dohuk Governorate has received little new foreign direct investment (FDI), following enactment of the Kurdistan Regional Government's (KRG) Investment Law in mid-2006. Although the law is materially more liberal than the Iraqi national investment law in several key respects, foreign investors remain scarce. Dohuk's weak infrastructure, relatively small population, and primitive banking system (representative of the banking situation throughout the KRG) pose material impediments to FDI. Senior economic officials in Dohuk recognize these constraints and express open disappointment with the FDI sums entering the governorate. Given Dohuk's constraints on economic development -- some self-created by the provincial government, some imposed from without, and some based on geography -- we believe Dohuk will attract relatively low levels of FDI and exhibit slower economic development than the remainder of the Kurdistan Region. END SUMMARY.

KRG Investment Law Offers Attractive Terms

¶3. (SBU) PRTOff met private sector leaders and senior government officials on August 16 in Dohuk City, in order to discuss the KRG Investment Law of July 2006, as well as the current economic state and outlook of the Dohuk Governorate. The KRG Investment Law has more attractive terms and conditions than both the Iraqi national investment law and similar laws in other developing countries. It allows 100 percent foreign ownership of land and does not prohibit ownership of banks and insurance companies, while the national investment law prohibits any degree of foreign ownership in all three areas. The KRG law also explicitly states that the regional government will bring basic services (water, electricity, sewage, public road access and telecommunications) on a cost-free basis up to the boundary of a foreign investor's project site, while the Iraqi national law makes no such offer. Both laws offer foreign investors ten years of income tax exemption, unhindered repatriation of project investment funds and accrued profits, and other attractive financial incentives.

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But Dohuk Governorate Fails to Lure Investment
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¶4. (SBU) Even with a liberal foreign investment law and consistently good security conditions, the Kurdistan region has not been able to attract the level of foreign investment the KRG expected. The Kurdistan Region's underdeveloped banking system hinders the ability of the Dohuk, Erbil and Sulaymaniah Governorates to attract significant foreign

direct investment, especially from countries other than Turkey (reftel). Problems in the banking sector -- and the cash-based economy that results from them -- continue to restrain capital investment and growth across virtually all economic sectors in the Kurdistan Region.

Constraints on FDI in Dohuk

¶5. (SBU) While Dohuk suffers from many of the same investment impediments affecting the entire Kurdistan Region, unique local constraints have hampered FDI even further. Compared with its larger sister provinces in the Kurdistan Region -- Erbil and Sulaymaniah -- Dohuk has a much smaller population, lacks an international airport, and remains more highly dependent upon the flows of electricity, goods and construction expertise from Turkey. NOTE: Turkish nationals account for approximately 80 percent of the FDI flowing into Dohuk Governorate. END NOTE.

¶6. (SBU) Dohuk Governorate's population of approximately 900,000 is by far the smallest of the KRG's three governorates. In addition, the province lacks, and has no firm plans to build, a commercial airport. This diminishes Dohuk's attractiveness to foreign investors, as they must travel by road into and out of Dohuk City. The trip typically entails a commercial flight to or from Erbil, and a three hour ride over back roads between Erbil and Dohuk City. The fastest route between Dohuk City and Erbil runs through Mosul, but investors consider it too dangerous to use.

¶7. (SBU) As Dohuk remains the Iraqi province most dependent on Turkish goods, investment and expertise, reports of a

potential Turkish cross-border operation disproportionately impact Dohuk's economy. Turkish government threats of major military operations against the Kurdistan Workers Party (PKK) present in Dohuk recently reduced the traffic of both goods and investment into the Kurdistan Region. According to a July 2007 report from Embassy Ankara, the government of Turkey reports that the flow of exports to northern Iraq slowed significantly in May and June, while Turkish media has reported that ten percent of Turkish companies in northern Iraq have left the region.

¶8. (SBU) Public and private sector leaders in Dohuk told PRTOff they need to diversify their province's economy away from dependence upon Turkish imports of all varieties, in order to decrease Turkey's economic and political leverage. However, efforts to source non-Turkish FDI and foster development of home-grown industries have generated little success. According to the Dohuk Governorate's Director General of Investment, Bakhtyar Ameen, about 80 percent of Dohuk's FDI continues to be sourced from Turkish investors who maintain 100 percent ownership of their projects. Ameen confirmed that "most (foreign) investors go to Erbil or Suly (Sulaymaniah)," as those governorates have larger populations and better developed infrastructures.

¶9. (SBU) Although crime rates are low and no coalition casualties have occurred in Dohuk since the start of Operation Iraqi Freedom, no insurers operate in Dohuk. FDI has been negatively impacted by this lack of basic insurance coverage. Investors are unable to locally procure the forms of coverage that often accompany FDI, including insurance against business interruption, commercial property damage, personal casualty, vehicle damage and other basic types of insurance.

Governorate Policies and Attitudes Limit FDI

¶10. (SBU) The same Dohuk government that seeks to attract FDI

hinders development of a thriving private sector and its related investment opportunities by serving as the province's largest employer. The Dean of Dohuk University's College of Administration and Economics, Dr. Khalil Besfki, told PRTOff that approximately 70 percent of the government must shift its expenditures toward improving the province's transportation and basic services infrastructure, while establishing mechanisms to transition government workers into private sector jobs. He said the Kurdistan Region's economic potential is also degraded by "a lack of economic planning" by the government, low participation of women in the workforce (less than 10 percent of working-aged women in all districts of the governorate, according to Besfki), and the government's inability to produce meaningful economic statistics that could guide potential investors or entrepreneurs.

¶10. (SBU) The Chairman of the Dohuk City Chamber of Commerce, Ayad Abdulhalim, wants Dohuk to use its mountains and relatively remote location to its advantage. He believes Dohuk's economic future lies in development of a tourism industry that caters to Arabs from southern Iraq and beyond. However, the KRG has formally relegated Arabic language instruction to a tertiary priority (after Kurdish and English) in primary and secondary schools, thereby degrading the ability of Dohuk citizens to attract and satisfy Arab tourists who would someday venture north to Dohuk's mountain resorts.

¶11. (SBU) While Arab investors from southern Iraq and the Persian Gulf states could potentially provide the non-Turkish FDI sought by the Dohuk Governorate, Ameen indicated to us that Arab investors are not highly welcomed. He claimed that Arab investors are only interested in the southern part of Iraq, due to language and cultural ties, and Ameen clearly preferred investment from Europe and the United States. He expressed frustration at being unable to attract such investment from the West, and he declared himself a "one man shop" in an understaffed office. He said, "Where are the American companies? Not a single one has invested here since the invasion in 2003."

Comment

¶12. (SBU) In Dohuk and the other two provinces of the Kurdistan Region, no U.S. or coalition force member has been killed by hostile fire since the March 2003 invasion of Iraq, while all other Iraqi provinces have witnessed deadly attacks. Despite this lack of violence against coalition

personnel and other foreign citizens, FDI inflows remain tepid and have disappointed the KRG. While publicly welcoming Turkish investors and construction companies, senior government officials in Dohuk privately express trepidation about the high impact of Turkish government actions and policies on the province. Efforts to diversify Dohuk's FDI inflows away from Turkey remain constrained by the province's relatively isolated location on the Turkish border, its limited and unstable basic infrastructure, and the province's unenthusiastic outreach to potential Arab investors. With its many challenges in attracting FDI -- some imposed from within, some from without, and some from its geographic isolation - we believe Dohuk's economic development and level of FDI investment will continue to lag behind those of its larger and better developed sister provinces of Erbil and Sulaymaniah. END COMMENT.

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